

Message Text

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TAGS: ECON ETRD CB TH

SUBJECT: MR III'S ECONOMY, AND CAMBODIA'S FOREIGN EXCHANGE PROBLEM

REF: A. STATE 252152 EXDIS 1973

B. STATE 2207

BEGIN SUMMARY. DIRECT EXPORTS TO THAILAND BY COMBODIAN SAPPHIRES AND OTHER PRECIOUS GEMSTONES FINANCE THE OVERLAND IMPORTATION FROM THAILAND OF A SIGNIFICANT VOLUME OF COMMODITIES FOR USE PRIMARILY IN NORTHWEST COMBODIA, AND, TO AN UNDERTERMINED EXTEND, PHNOM PENH. NO RELIABLE ESTIMATES OF THE VOLUME OF THIS TRADE EXIST BUT THE FLOW OF GOODS APPEARS VIABLE AND REASONABLY BALANCED WITH ONLY A RELATIVELY THIN MARGIN LEFT FOR CAPITAL FLIGHT.

AT CURRENT PRODUCTION LEVELS, THE GEM TRADE DOES NOT APPEAR TO CONSITITUE AN IMMEDIATELY AVAILABLE FOREIGN EXCHANGE RESOURCE BECAUSE MOST OF ITS EARNINGS ALREADY FINANCE NEEDFZ IMPORTS. HOWEVER, WITH PROPER MANAGEMENT AND EFFECTIVE GOVERMENT POLICIES, THERE APPEARS TO BE A POTENTIAL FOR INCREASED EXTRACTION AND EXPORT OF PRECIOUS STONES. GIVEN SECURITY PROBLEMS, KHMER BUREAUCRATICS, QUESTIONS OF CORRUPTION AND INTERNAL START-UP TIME, THIS

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RESOURCE WILL TAKE TIME (AT LEAST A YEAR) TO MAKE MORE THAN

A MARGINAL CONTRIBUTION TO THE SOLUTION OF THE FX PROBLEM. NONETHELESS WE BELIVE WE SHOULD FOLLOW-UP AND STUDY THE PROSPECTS IN DEPTH. END SUMMARY.

I - SCOPE OF STUDY

A. PURPOSE

1. IN RESPONSE TO REFTELS, AN EMBASSY OFFICER FROM PHNOM PENH (TIMOTHY CARNEY) AND ONE FROM BANGKOK (HERVEY CLARK) EXPEND FIVE DAYS IN MR III SURVEYING TRADE PATTERNS AND MONETARY FLOWS TO ASCERTAIN WHAT FINANCES THE OVERLAND IMPORTS FROM THAILAND INTO AND THROUGH MR III AND HOW THESE TRANSACTIONS TAKE PLACE; TO ESTIMATE THEIR EFFECTS ON THE CAMBODIAN ECONOMY AS A WHOLE; AND TO SEE HOW MR III COULD INCREASE ITS CONTRIBUTIONS TO COMBODIA'S FOREIGN EXCHANGE EARNINGS AND THE ECONOMIC SUPPORT OF THE CAPITAL. WE DID NOT EXAMINE THE RICE TRADE OR THE ECONOMIC RELATIONS BETWEEN THE KHMER COMMUNISTS (KC) AND THE FRIENDLY AREAS.

B. SCOPE - SOURCES OF INFORMATION

2. IN THREE DAYS IN BATTAMBANG AND ONE EACH IN MONKOLBORIE (LOGGING) AND BPAILIN (THE GEM PRODUCING AREA), WE VISITED GOVERNMENT OFFICIALS (FORESTRY, FISHING, CUSTOMS, AND RAILROAD); PRIVATE BUSINESSMEN (LUMBERMEN, GEM MERCHANTS, TAXI OWNERS, AND SMALL BUSINESSMEN); MARKETS IN PAILIN, BATTAMBANG AND PHNOM PENH; BANKERS IN BOTH BATTAMBANG AND PAILIN; OFFICIALS OF THE CAMBODIAN NATIONAL GEM EXPORTATION ORGANIZATION IN BOTH PHNOM PENH AND PAILIN; AND A LEADING AMERICAN WHOLESALE GEM EXPORTER IN BANGKOK. IN ADDITION, EMBASSY BANGKOK SENT AN EXPERIENDED THAI EMPLOYEE TO ARANYAPRATHET, CHANTABURI, TRAD, AND POACHINBURI PROVINCES IN THAILAND, AND POIPET, CAMBODIA. THIS REPORT INCLUDES THE RESULTS OF HIS MEETINGS WITH RTG OFFICIALS AND PRIVATE MERCHANTS IN THESE PLACES.

SO II. - PATTERNS OF TRADE

A. OVERLAND EXPORTS AND IMPORTS TO AND FROM THAILAND

3. SAPPHIRES AND OTHER PRECIOUS GEMSTONES MOVE FROM THE PAILIN AREA OF MR III DIRECTLY OVER THE BORDER AND INTO CONFIDENTIAL

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THAILAND ON A NEW ROAD ACROSS O LAC. A REC TIVELY SMALLER AMOUNT PROBABLY ALSO MOVES TO BATTAMBANG AND PHNOM PENH. EXCEPT FOR A LIMITED AMOUNT OF HOARDING BY RICH KHMER, VIRTUALLY ALL CAMBODIAN GEMSYQES SELL FOR FOREIGN EXCHANGE, PRIMARILY BAHT, AND MEARLY ALL SALES ARE OUTSIDE THE NATIONAL FOREIGN EXCHANGE CONTROL AND ACCOUNTING MECHANISMS.

4. CAMBODIA ALSO EXPORTS HIDES, ORANGES, SCRAP BRASS,

AND HARDWOODS, BUT THE AGGREGATE VALUE OF THESE PRODUCTS IS SMALL COMPARED TO THE GEMSTONES. (HOWEVER, AT LEAST ONE 15,000 TON SHIPMENT OF SCRAP IRON HAS MOVED RECENTLY FROM CAMBODIA TO THAILAND.:(

5. CAMBODIAN IMPORTS OVERLAND FROM THAILAND INCLUDE SUGAR, SALT, CEMENT, RICE, CORRUGATED ROOFING SHEETS, SYNTHETIC FIBRE AND MIXED SYNTHETIC/COTTON CLOTH, ALUMINUM COOKWARE, MEDICAL SUPPLIDE, AND OTHER HOUSEHOLD NECESSITIES IN ADDITION TO PETROLEUM PRODUCTS, CONSTRUCTION MATERIALS AND HEAVY MACHINERY DESTINED FOR USE IN MR III OR IV.

6. WHILE MR III GETS FIRST CRACK AT THAI EXPORTS AT LOWER PRICES, SIGNIFICANT QUANTITIES OF THESE GOODS ALSO SUPPLY THE PHNOM PENH MARKET. CAMBODIA NOW IMPORTS ALMOST ALL OF ITS SUGAR; IT APPARENTLY COMES IN OVERLAND FROM THAILAND WITHOUT IMPORT LICENSING OR CIP/ESF FINANCING. THAI CLOTH,

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CEMENT, AND ROFFING SHEETS ALSO MAKE THEIR WAY TO THE PHNOM PENH MARKET IN SIGNIFICANT QUANTITIES.

7. NORTHWEST CAMBODIA RECEIVES PHARMACEUTICALS FROM PHNOM PENH AS WELL AS FRENCH AUTOMOBILE AND BICYCLE SPARE PARTS, ELECTRONIC GOODS (WHICH ARE PROBABLY AS EXPENSIVE IN THAILAND

AS THOSE LEGALLY IMPORTED INTO CAMBODIA), AND OTHER MINOR CONSUMER GOODS.

C. HOW THE TRADE IS FINANCED--MOVEMENTS OF MONEY AND CREDIT

8. MOST OF THE GEMS FROM PAILIN ARE SOLD FOR PROMISSORY CHITS, OR IOU', WHICH ARE USUALLY REDEEMABLE IN BANGKOK FOR BAHT OR OTHER FOREIGN EXCHANGE. MUCH OF THIS MONEY IS THEN CONVERTED INTO MERCHANDISE WHICH IS SENT BY RAIL OR TRUCK TO ARANYAPRATHET, ON THE THAI/CAMBODIAN BORDER, FOR EXPORT TO CAMBODIA. OTHER CHITS GO FROM PAILIN TO BATTAMBANG AND ARE LATER USED TO BUY MERCHANDISE IN ARANYAPRATHET. MUCH OF THE CURRENTY CONVERSION TAKES PLACE ON PAPER, BUT THERE ARE EXCHANGE HOUSES ON THE BORDER NEAR PAILIN AND ALSO IN ARANYAPRATHET.

9. A SEIRATE CIRCULATION OF RIEL CHITS TAKES PLACE BE-
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TWEEN PAILIN AND BATTAMBANG. A GEM DEALER FROM BATTAMBANG WILL BUY STONES IN PAILIN AND PAY BY CHIT. THE PAILIN DEALER THEN SENDS THIS CHIT BACK UP TO BATTAMBANG AND RE-DEEMS IT FOR FOOD AND GOODS WHICH ARE SHIPPED TO PAILIN. WHEN THESE ARE SOLDIN THE MARKET, THE PAILIN GEM DEALER, WHO IS ALSO EITHER A GENERAL TRADER OR ASSOCIATED WITH ONE, REPLENISHES HIS CASH BALANCES. STONES GO TO BATTAM-BANG AND GOODS TO PAILIN, BUT PHYSICAL EXCHANGE OF RIELS BETWEEN THE TWO TOWNS APPEARS LIMITED.

D. APPROXIMATE MAGNITUDES OF VARIOUS SECTORS OF THESE TRADING
TRADING PATTERNS

(1) EXPORTS/IMPORTS

10. ESTIMATES OF THE GEMSTONE EXPORTS FROM CAMBODIA VARY WIDELY, RANGING FROM 2.5 TO 20 MILLION DOLLARS OR MORE PER YEAR. THE MORE CREDIBLE SOURCES INDICATE THAT IT IS BETWEEN 8 TO 12 MILLION DOLLARS ANNUALLY. A MAJOR DIFFI-CULTY IN MAKING AN ACCURATE ESTIMATE IS THE PROGRESSIVE IN-CREASE IN THE STONES' VALUE AS THEY MOVE TO BANGKOK AND BE-YOND. THUS VARIOUS INFORMANTS GIVING DIFFERENT FIGURES MAY BE REFERRING TO VALUES AT DIFFERENT STEPS ALONG THE WAY. AT THIS POINT, WE DO NOT HAVE A CLEAR PICTURE OF JUST HOW MUCH A GIVEN STONE INCREASES IN VALUE AT EACH STAGE, AND CANNOT THEREFORE TRANSLATE DIFFERING FIGURES IN TO A COMMON REFERENCE VALUE.

11. IMPORTS FROM THAILAND THAT THE GEM TRADE FINANCES ARE EQUALLY HARD TO ESTIMATE. A "TROC-TAXE" SYSTEM PERMITS UNLICENSED IMPORTS ACROSS CAMBODIA'S FRONTIERS, BUT CON-

SIDERABLE SMUGGLING EXISTS WITH A RESULTANT OFFICIAL IGNORANCE OF, OR WILL TO CONCEAL, THE REAL FIGURES.

12. BOTH THAI AND GKR FIGURES INDICATE THAT CAMBODIA IMPORTS ABOUT 400,000 DOLLARS WORTH OF CEMENT A YEAR FROM THAILAND. THOUGH THE FIGURES ARE LESS SURE, WE BELIEVE THAT ABOUT \$200,000 WORTH OF SALT COMES IN FROM THAILAND ANNUALLY.

13. WE HAVE NO FIGURES, EVEN APPROXIMATE, FOR SUGAR IMPORTS.
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PORTS. MOST OF IT COMING FROM THAILAND APPEARS TO BE SMUGGLED IN FROM ARANYAPRATHET TO POIPET, MUCH OF IT BY HORDES OF CARRIERS BEARING ONE BAG APiece IN KNAPSACKS. RAIL OFFICIALS IN BATTAMBANG SAY THAT SINCE THE SUGAR IS CONTRABAND SMUGGLERS DO NOT SHIP IT BY RAIL. A TAXI DRIVER WHO PILES FROM BATTAMBANG TO POIPET, HOWEVER, SAID THAT IT WAS EASIER TO SMUGGLE THE SUGAR IN RAIL CARS AND THAT COOLIES TRANSFERRED FROM THAI TO CAMBODIAN BOX CARS ON ADJACENT SIDINGS IN THE POIPET STATION.

14. ALL WE REALLY KNOW IS THAT NEARLY ALL CAMBODIA'S SUGAR COMES IN FROM THAILAND; THAT SUGAR COSTS ABOUT \$300 PER TON; THAT CAMBODIA USES A LOT OF SUGAR; AND THAT NO SIGNIFICANT FIGURES FOR SUGAR APPEAR ON ANY OF CAMBODIA'S FOREIGN EXCHANGE ACCOUNTS. SUGAR THEREFORE SEEMS TO CONSTITUTE A SIGNIFICANT PORTION OF THE IMPORTS THAT THE GEM TRADE FINANCES.

(2) NORTHWEST CAMBODIA/PHNOM PENH

15. MR III AND IV SEND MUCH MORE DOMESTICALLY PRODUCED FOODSTUFFS (RICE, FISH, PORT, AND FRUITS AND VEGETABLES) TO PHNOM PENH THAN THE AREA RECEIVES FROM PHNOM PENH IN DOMESTIC GOODS (PHARMACEUTICALS, BATTERIES, AND OTHER SMALL CONSUMER PRODUCTS). IT IS LESS EASY TO ESTIMATE WHETHER MR III SENDS MORE IMPORTED (THAI) GOODS TO PHNOM PENH THAN IT RECEIVES IN FOREIGN GOODS IMPORTED THROUGH PHNOM PENH.

16. PHNOM PENH'S POPULATION, HOWEVER, NEEDS THE IMPORTED

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GOODS IN THE CAPITAL GETS FROM MR III MORE THAN THE PEOPLE
IN MR III NEED FOREIGN GOODS THEY PURCHASE FROM PHNOM PENH.
IN A PINCH, MR III COULD RELY TOTALLY ON IMPORTS FROM
THAILAND, WHEREAS PHNOM PENH HAS NO VIABLE ALTERNATIVE TO
ITS PRESENT TRADE PATTERNS WITH MR III AND THAILAND. THIS
LATTER POINT IS EVEN MORE TRUE SINCE THE COMMUNISTS' RE-
CENT SEIZURE OF COMBODIA'S ONLY CEMENT PLANT.

III. - EFFECTS ON THE KHMER ECONOMY AS A WHOLE

A. SUPPLEMENT IMPORTS -- SUPPLIES SOME
GOODS EXCLUSIVELY

17. MR III'S INDEPENDENT FOREIGN EXCHANGE EARNING CAPA-
BILITY SERVES TO CUPPLEMENT CAMBODIA'S FORMAL FOREIGN EX-
CHANGE ACCOUNTS. THE GOODS COMING IN THROUGH NORTHWEST
CAMBODIA RAISE THE OVERALL LIVING STANDARD NOT ONLY IN
MR III BUT IN SIEM REAP (MR IV) AND THROUGH TO PHNOM PENH
AS WELL

18. THE SUGAR THAT COMES IN FROM THAILAND APPARENTLY
SUPPLIES THE ENTIRE COUNTRY. ALL OF IT IS BROUGHT WITH
FOREIGN EXCHANGE THAT IS EARNED THROUGH THE EXPORT OF
THE GEMSTONES AND THE OTHER MINOR EXPORTS FROM MR III.
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THE LARGE QUANTITIES OF TEXTILES FROM THAILAND, MUCH OF IT
SYNTHETIC AND SYNTHETIC BLENDS THAT ARE NOT PRODUCED IN

CAMBODIA, ARE LIKEWISE NOT IMPORTED THROUGH CIP/ESF. THIS CLOTH IS PLENTIFULLY EVIDENT IN PHNOM PENH AS WELL AS IN BATTAMBANG, PAILIN, PURSAT, KOMPONG CHHNANG.

B. ENABLES CAPITAL FLIGHT

19. BY PROVIDING AN UNHARNESSED FOREIGN EXCHANGE EARNING CAPABILITY, THE GEM TRADE ENABLES COMBODIANS TO EXPORT CAPITAL. IT IS IMPOSSIBLE TO ESTIMATE THE EXCESS OF GEM-STONE EXPORTS OVER THE VALUE OF MERCHANDISE IMPORTS THROUGH MR III. HOWEVER, WE BELIEVE THE CAPITAL FLIGHT USING THIS EXCESS IS SIGNIFICANT ENOUGH TO KEEP UNDUE PRESSURE OFF THE ESF/NMC, AND THUS THE OFFICIAL RATE.

C. INDICATES THE RIEL'S VALUE

20. THE FOREIGN DEMAND FOR PAILIN GEMS AND OTHER CAMBODIAN PRODUCTS GENERATES A CONTINUING DEMAND FOR RIELS FOR PURCHASE OF THE EXTRACTED PRODUCTS. THIS LATTER DEMAND DEFINES THE MARKET VALUE OF THE RIEL, AND THEREBY SHOWS CONCLUSIVELY THAT THE OFFICIAL EXCHANGE RATE CONTINUES TO OVERVALUE THE RIEL.

D. FINANCES A RIEL BUILDUP

21. THE WEALTH THAT HAS ACCUMULATED AS A RESULT OF THE LARGE EXPORT/IMPORT TRADE TAKING PLACE IN MR III HAS REPORTEDLY FOUND ITS WAY INTO THE HANDS OF THE SENIOR MILITARY LEADERS IN PHNOM PENH. BUT THESE LARGE RIEL STORES HAVE NOT MANIFESTED THEMSELVES IN INCREASED PER CAPITA LIQUIDITY. WHAT APPEARS TO HAVE HAPPENED IS THAT THROUGH PARTNERSHIPS IN TRADE AND THE UPWARD PERCOLATION OF THE PROFITS OF CORRUPTION, A RELATIVELY FEW PEOPLE HAVE COME INTO POSSESSION OF CASH HOARDS THAT ARE SO LARGE THAT THE OWNERS HAVE NO VIABLE ALTERNATIVE BUT TO SIT ON THEM. POSSIBLY THE RICH CONTINUE TO HOLD THESE CASH HOARDS FOR FEAR OF DISCOVERY IF THEY SURFACE AND PERHAPS ALSO BECAUSE OF POOR MARKET INFORMATION. THE LOCUS OF THE RIEL BUILDUP IS STILL AN OPEN QUESTION REQUIRING FURTHER RESEARCH.

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22. IF FOR ANY REASON THIS LIQUIDITY SHOULD ENTER THE MARKET (E.G. TO BUY COMMODITIES FOR HOARDING) IT COULD DRIVE PRICES UP STEEPLY AND OBLITERATE THE ALREADY STRAINED

PURCHASING POWER OF THE MIDDLE AND LOWER CLASSES.

IV. - MR III'S POTENTIAL FOR AIDING THE ECONOMY AS

A WHOLE

A. RICE

23. THE RICE TRADE IS OUTSIDE THE SCOPE OF THIS STUDY.

B. GEMS

24. AT PRESENT LEVELS OF EXPLOITATION, WE BELIEVE THAT THERE IS PROBABLY NOT TOO MUCH MARGIN OF CAPITAL FLIGHT) THAT COULD BE DIVERTED INTO GKR FX. HOWEVER, THE EXPLOITATION OF THE GEM FIELDS IS PRESENTLY CRUDE, INEFFICIENT, AND SMALL SCALE, AND GOVERNMENT CONTROL OF THE EXPORTS TO THAILAND IS NON-EXISTENT. WITH BETTER MANAGEMENT, INVESTMENT IN MODERN MINING MACHINERY, BETTER STONE CUTTING, AND GREATER INCENTIVES TO EXPORT STONES THROUGH FORMAL CHANNELS, WE BELIEVE CAMBODIA COULD INCREASE ITS FOREIGN EXCHANGE EARNINGS ENOUGH TO CONTINUE THE NECESSARY CROSS BORDER TRADE WITH THAILAND, AND TO FINANCE A SIGNIFICANT QUANTITY OF IMPORTS THROUGH PHNOM PENH AS WELL.

25. RELIABLE ESTIMATES OF HOW MUCH FOREIGN EXCHANGE THE GEM FIELDS MIGHT EARN AND HOW FAST CANNOT BE FOUND. NOTWITHSTANDING THE GEM TRADE'S PRESENT SLUMP BECAUSE OF THE MIDDLE EAST WAR AND JAPAN'S FUEL PROBLEMS, THE PROMISE IS SUFFICIENT THAT WE SHOULD INSIST THAT THE GKR SEEK EXPORT ADVISE IMMEDIATELY. THE GKR SHOULD CONSIDER FRANCHISING A PRIVATE CONCERN CAPABLE OF DEVELOPING THE GEM FIELDS AND TRAINING KHMER LAPIDARIES SO THAT THE STONES WILL ATTAIN MAXIMUM VALUE BEFORE LEAVING CAMBODIA. ONE FIRM WOULD ALSO HAVE TO HAVE EXCLUSIVE GEM EXPORT FRANCHISE THROUGH FORMAL EXCHANGE CHANNELS. PRESIDENT LON NOL TELLS THE CHARGE THAT HE WOULD WELCOME SUCH AN INITIATIVE.

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26. AS FAR AS WE CAN NOW ASCERTAIN, THE DECISIONS THAT SUCH A PROPOSAL WOULD REQUIRE OF THE GKR ARE WITHIN ITS ABILITY TO MAKE AND IMPLEMENT. INASMUCH AS THE LARGER SCALE COMMERCIAL EXPLOITATION OF THE FIELDS WOULD BE A NET ADDED RESOURCE, AND NOT MERELY A RECAPTURING INTO FORMAL CHANNELS OF AN EXISTING BLACK MARKET TRADE, IT APPEARS THAT THE GKR COULD TAKE THE NECESSARY DECISIONS WITHOUT STEPPING UNDULY ON THE TOES OF THOSE WHO HAVE A LARGE ECONOMIC STAKE IN THE PRESENT SET-UP. WE ARE SENDING BY SEPTTEL A TENTATIVE LIST OF THE KINDS OF ACTIONS THE GKR WOULD HAVE TO TAKE TO ATTRACT AND BENEFIT FROM A FRANCHISED PRIVATE INVESTOR. ENDERS

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